

INTERNAL REVENUE SERVICE

RETURN PREPARER REVIEW PUBLIC FORUM

Internal Revenue Service
Washington, D.C.

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P R O C E E D I N G S

9:03 a.m.

Welcome

COMMISSIONER SHULMAN: Good morning,
everybody.

I have the honor of kicking this forum off
and introducing my colleagues and then I'm going to
turn it over to Karen Hawkins who will introduce our
distinguished panelists.

Let me first welcome everybody in the
audience for coming and participating in this public
forum reviewing tax return preparers and what more the
Service could potentially do around ensuring the
integrity of the preparer community.

Let me also just thank our distinguished
panelists for spending the time here. Some of you
traveled far, some of you drove down, but we'll very
much benefit from your insights and look forward to the
dialogue that we have.

Let me just also acknowledge Paul Cherecwich
who is in the audience who's Chairman of the IRS
Oversight Board and Ed Eck, I saw back there, who's an
Oversight Board Member, and thank them for supporting
this effort and coming to this forum.

Let me say a couple things to kick this off.

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1 One is this is a very important issue for us of how we
2 work with the paid preparer community and a lot of
3 people have asked why I and our senior team decided to
4 put this on the front burner this year and I will tell
5 you the reason for this is the tremendous change in the
6 way that taxes are prepared and the tax system works in
7 this country.

8 I often say that there's this image of people
9 pulling out their shoebox with all their receipts some
10 time before April 15th and scribbling out their return
11 and wrestling with the complex Tax Code and complex tax
12 forms and that's really an image of the past.

13 Today, 90 percent of individuals use a paid
14 preparer or software to prepare their tax returns and
15 what this intuitively means to me and empirically, I
16 think, means to the system is that, while the IRS is
17 responsible for making sure that voluntary compliance
18 works in this country, we need to make sure that the
19 preparer community is an integral part of our strategy
20 to ensure the voluntary compliance is successful in
21 this country and we collect the taxes that are owed.

22 This review is aimed to have us understand
23 the preparer community better, ensure that preparers
24 are providing good quality ethical service to customers
25 who, whether we like it or not, have to wrestle with

1 the complex Tax Code and rely on professionals to meet
2 their tax-paying obligations, and also to make sure
3 that preparers are part of the solution to ensure that
4 we collect the proper amount of tax to fund the Federal
5 Government.

6 If you fast forward, I committed by the end
7 of this year to make a set of recommendations. Some of
8 those will be things that we can do ourselves under our
9 authority but some of those may need legislative
10 changes and so I'm going to be sending recommendations
11 to Treasury Secretary Geithner, President Obama about
12 the overall comprehensive approach that we have and
13 where we're going to go forward.

14 Let me stress that all ideas are welcome at
15 the table. We recognize that these are nuanced issues.
16 We still have made and I've made no conclusions about
17 what those recommendations will be. We're now
18 midstream into the process, but it's still early and
19 that's why we're having these public forums and making
20 sure that we engage the best people we can around
21 giving us input.

22 Today, we have representatives from the
23 Treasury Inspector General for Tax Administration, the
24 Government Accountability Office, the States of
25 California, Maryland, Oregon, and New York, who've been

1 in the forefront of looking at ways to ensure preparers
2 meet high ethical standards.

3 We also need you to weigh in. There are
4 comment cards out there and some of our core team, when
5 we're done, will be staying around and so we'll look
6 forward to continuing this dialogue after we have the
7 public portion.

8 Let me just introduce Mark Ernst, who is
9 Deputy Commissioner for Operations Support, and Karen
10 Hawkins, who is Director of Office of Professional
11 Responsibility. I've asked them to lead this effort
12 with me as we look at this.

13 Mark has a deep background as a business
14 executive in the tax preparation industry, so
15 understands the industry well. Karen was scheduled to
16 become Chair of the American Bar Association this year,
17 until we were lucky enough to recruit her, and has a
18 lot of experience with the tax and preparer community.

19 So again, let me thank you for coming today
20 and let me turn it over to Karen who will take it from
21 here.

22 Introduction of Panel Members

23 MS. HAWKINS: Thanks, Commissioner. Can you
24 all hear me? Yeah. Okay. I never know about these
25 levelers.

1 I'm just going to quickly run down the panel
2 and tell you who you're looking at and then we'll come
3 back and we'll start with each panelist's five-minute
4 statement. We'll go through the entire panel with the
5 statements and then, as is the Commissioner's
6 prerogative, he will start the questioning, and at some
7 point he'll let Mark and I participate in that.

8 (Laughter.)

9 MS. HAWKINS: Immediately next to the podium
10 is Mike Brostek, who is the Director of Strategic
11 Issues at GAO. Next to Mike is another Mike, Mike
12 McKenney, who is the Assistant Inspector General for
13 Audit with TIGTA.

14 Next to Mike is Celeste Heritage. Celeste is
15 the California Tax Education Council or CTEC
16 Administrator in California. Next to Celeste is Ruth
17 Moore. Ruth is the Manager of Fraud and Discovery
18 Section in the Filing Compliance Bureau of the
19 Franchise Tax Board in California.

20 Next to her is Wallie, Wallace, sorry,
21 Eddleman, who's the Assistant Director for Legal for
22 the Comptroller of Maryland in the Revenue
23 Administration Division. Next to him is Jamie
24 Woodward, who is the Acting commissioner for the
25 Department of Tax and Finance in the State of New York,

1 and last but certainly not least is Ron Wagner, who is
2 the Executive Director of the State Board of Tax
3 Practitioners in Oregon.

4 So we're going to start with Michael and
5 Michael is, in his position at GAO, is responsible for
6 reviews that relate to the management of the IRS and
7 its various programs and how well the federal tax
8 policy objectives are achieved. He's been involved
9 before with other looks at how the Internal Revenue
10 Service addresses its preparer community.

11 So we're looking forward to hearing your
12 comments, Michael.

13 U.S. Government Accountability Office (GAO)

14 MR. BROSTEK: Okay. Well, thank you for
15 inviting GAO to participate in the panel today. It's a
16 very important topic and I look forward to the
17 discussion.

18 I won't review a lot of facts because I'm
19 sure that everybody here is aware of some of the
20 baseline. As you were saying, Mr. Commissioner, 60
21 percent or more individual tax returns are prepared by
22 paid preparers. So their performance is extremely
23 important to the tax administration system.

24 IRS officials sometimes refer to the paid
25 preparer community as partners in tax administration.

1 So if you're a partner in a law firm, it's really
2 important that you perform well and if you don't
3 perform well, well, there might be some consideration
4 about whether you ought to remain in the firm.

5 What do we know about performance? Well, we
6 know that a lot of preparers work very hard, very
7 diligently and very skillfully to help individuals
8 decipher a complex Code and report their tax
9 obligations properly.

10 But there are also a number of indications
11 that the paid preparer community does face some
12 performance challenges. For instance, in 2002, we
13 reported that about 2.2 million taxpayers used the
14 standard deduction when they would have been better off
15 itemizing deductions.

16 Those taxpayers, we estimate, overpaid by
17 around a billion dollars and half of them used paid
18 preparers. Whether to take a standard deduction or
19 itemized deductions is not one of the complex tax
20 issues, yet there were an awful lot of errors being
21 made.

22 In 2006, we did an undercover visit to 19
23 paid preparers in a major metropolitan community. All
24 these preparers were employed by major chains. All 19
25 made errors. Some of those errors were relatively

1 small, but a number of them were also quite
2 significant, and they could have exposed a taxpayer to
3 significant enforcement actions on IRS's part, possibly
4 penalties, certainly time taken out of their lives to
5 try to deal with the problems that the paid preparer
6 contributed to.

7 In fact, 10 of the 19 paid preparers told us
8 we did not have to report cash side income to IRS. We
9 were very open. We had these side jobs. We earned
10 income, and we were told that was really our decision.
11 There was no way IRS would know. So it was up to our
12 good conscience to decide whether we wanted to report
13 that.

14 News media, our colleagues in TIGTA, the
15 Department of Justice, New York law enforcement, and
16 others have all done similar undercover visits to paid
17 preparers and found performance that also was not
18 always stellar, shall we say.

19 Out of our work, we recommended that IRS
20 undertake some studies to try to determine how well
21 this community performs to get a better sense of what
22 we found in a small set of visits was more typical.

23 In March of last year, we recommended that
24 IRS prepare a plan for assigning individual
25 identification numbers to each paid preparer and that

1 number would be on the tax return that they prepare and
2 will be transcribed into databases by IRS. We think
3 that's very foundational to any effort really to help
4 improve the performance of this community.

5 By knowing who prepared the return, IRS could
6 do research to identify preparers or even specific tax
7 issues that are not being handled well. Perhaps even
8 real time during the tax season, IRS do educational or
9 enforcement out reach to try to deal with the issues
10 that are found, but being able to identify the paid
11 preparer is really very foundational.

12 We also last year did some work looking at
13 the California and Oregon paid preparer regulatory
14 schemes. What we tried to do is model all the factors
15 that we thought might influence the accuracy of a
16 return and that we could measure and control for those
17 so we could try to determine whether the regime made
18 any difference.

19 We found that the Oregon regime was
20 associated with greater federal tax return accuracy.
21 Those returns were more accuracy than the average
22 returns in the country.

23 Our work was not sufficient to conclude that
24 it was the regime that contributed to that accuracy.
25 There's a logic behind it, but we can't conclude that

1 for sure because we couldn't measure all the factors
2 that contributed to improved accuracy and there are
3 states who don't have regulatory regimes who also have
4 returns that are more accurate than average for the
5 country.

6 Nevertheless, we concluded that if even a
7 small portion of that increased accuracy was due to the
8 return on a cost-benefit basis, adopting an Oregon
9 style return could be very competitive with IRS's
10 overall efforts to improve tax return accuracy and,
11 indeed, with some of these specific targeted efforts
12 that IRS has.

13 Therefore, we concluded that Congress should
14 review the facts that we presented and make its own
15 judgment about whether a regime like Oregon's should be
16 extended to the country.

17 In closing, paid preparers are extremely
18 important to the tax system. The system probably could
19 not perform without them these days. However, their
20 performance is extremely important to both the taxpayer
21 who can suffer really significant adverse consequences
22 to poor performance and to the tax administration
23 system.

24 I sometimes think of paid preparers as akin
25 to promoters and that's normally in the tax world

1 thought of as a pejorative term, but it's not
2 necessarily the case. Paid return preparers can be a
3 promoter of good for tax administration if they're
4 skillful and ethical, but they can be significant
5 promoters of bad results if they aren't.

6 MS. HAWKINS: Thanks very much, Michael.
7 We're going to look forward to asking you some more
8 questions about some of your comments later.

9 Next up is Mike McKenney. Mike is the, as I
10 told you, the Assistant Inspector General for Audit at
11 TIGTA. He's been involved extensively in audits
12 involving the things that we would be interested in in
13 managing our paid preparer program, frivolous returns,
14 questionable refund programs. He's also been involved
15 in audits that involve the Office of Appeals, Taxpayer
16 Advocate, and the Office of Professional
17 Responsibility.

18 So Michael.

19 Treasury Inspector General for Tax Administration
20 (TIGTA)

21 MR. MCKENNEY: Thank you. Well, on behalf of
22 the Inspector General, J. Russell George, I'd like to
23 thank the Commissioner for the opportunity to
24 participate in this panel looking at the tax return
25 preparer review.

1 I wanted to give you a little bit of
2 background for those who may not be familiar with our
3 involvement in the issues related to tax preparers.

4 The Office of the Inspector General was
5 created as a result of the IRS Restructuring and Reform
6 Act of 1998 really in order to provide oversight of IRS
7 activities which involves promoting the economy,
8 efficiency, and effectiveness of tax administration,
9 and also preventing fraud, waste, and abuse.

10 Both our Office of Audit and our Office of
11 Investigations both play a significant role in the
12 government's oversight of tax preparers.

13 The Office of Audit reviews IRS's oversight
14 of tax preparers and in the last -- since last July,
15 we've looked at four different areas related to tax
16 preparers. One is the Return Preparer Program which is
17 the enforcement side of the IRS's effort in this area.

18 We've also looked at the accuracy of returns
19 prepared by tax preparers. We've looked at the
20 complaint process for taxpayers who complain about
21 preparers, and we've also looked at the information
22 systems and how IRS identifies and tracks paid
23 preparers.

24 Our Office of Investigation investigates any
25 attempts to impede tax administration and it routinely

1 investigates preparers who engage in these schemes to
2 defraud their clients or the government and that
3 involves the types of preparers who overstate their
4 qualifications and that includes preparers who may
5 falsely claim to be CPAs, attorneys, or enrolled
6 agents, preparers who steal clients' tax payments or
7 tax refunds as well as preparers who may impersonate
8 the IRS or misuse the IRS's seal or logo.

9 These are all activities of damage of the tax
10 administration system and we'll work closely with the
11 IRS as it attempts to obtain any regulations or
12 implements any of the laws in that area.

13 In relation to standards and improved
14 oversight, we believe that the current situation of
15 lack of national standards is a cause for concern
16 because unqualified, unethical preparers can cause
17 enormous damage to the tax administration system.

18 We've recently, in the 2008 filing season, we
19 did anonymous visits to tax preparers where our
20 auditors had to visit 28 tax preparation businesses to
21 have tax returns prepared and we found that there was a
22 substantial number of inaccurate returns prepared.
23 Overall, we found that there was only 39 percent of the
24 returns we had prepared that were accurate and of the
25 61 percent that were inaccurate, about two-thirds were

1 human error or misinterpretation of the tax law, but
2 about a third of those were reckless or intentional
3 misconduct.

4 We also found that preparers didn't follow
5 the requirements. For example, preparers are required
6 to exercise due diligence in determining whether
7 taxpayers are eligible for their earned income tax
8 credit, but in none of the cases where it was
9 applicable did they exercise that due diligence.

10 Preparers are also required to sign their
11 return and furnish their identification number, but in
12 several instances, they did not do that.

13 Furthermore, none of the preparers prepared
14 the Schedule C business income and expenses returns
15 correctly and there was many other types of errors,
16 notwithstanding the fact that all the preparers we
17 visited used commercial software.

18 While a system of national standards and
19 testing wouldn't necessarily have prevented all those
20 problems, we believe it would have reduced the rate of
21 inaccuracy. Our experience, looking at the VITA sites,
22 I think shows that an increased emphasis on standards
23 testing and other tools has really helped improve the
24 VITA Program.

25 When we first started looking at the VITA

1 Program in 2004, there was a zero percent accuracy rate
2 and over time, with increased emphasis, it's improved
3 to 59 percent this year. But the tax preparation
4 industry, the emphasis on tax preparation industry
5 would yield, we think, a greater benefit to the tax
6 administration because about 87 million returns are
7 prepared by tax preparers versus about 3.5 million
8 returns by volunteers.

9 We've conducted a number of reviews where
10 we've looked at the IRS's ability to track paid
11 preparers as well as practitioners and we've called on
12 the IRS to use a single federal identification number
13 since 2006 and we recently again reiterated that we
14 believe this is an important way to track and
15 understand the population of paid preparers.

16 When we looked at the current situation, over
17 60 percent of preparers use different numbers. For
18 example, they'll use social security numbers on some
19 tax returns they prepare and they'll use their preparer
20 taxpayer identification numbers on other returns they
21 prepare and some of them will use the employer
22 identification number instead of those and about six
23 percent of the ones we looked at, you couldn't identify
24 because they used an invalid preparer identification
25 number.

1 There's a lot of different systems IRS has.
2 It has preparer information, and without some kind of a
3 standard or single identification number, it makes it
4 very difficult for those systems to work effectively.
5 So we believe that is an important aspect of your
6 current effort to make sure that you have a standard
7 identification number to make sure all the systems
8 interrelate to each other.

9 One of the things that came up in the last
10 return preparer panel that I think is important and a
11 number of panelists said this, that they believe the
12 responsibility for oversight should be consolidated
13 within the Office of Professional Responsibility, and
14 we believe that that recommendation has merit.

15 A recent audit we did on the complaint
16 process shows why any ambiguities of jurisdiction can
17 cause some problems. In the complaint area, numerous
18 IRS functions handle complaints against tax preparers
19 and as such, it's not -- many of the complaints aren't
20 well tracked. It's hard for the IRS to know how many
21 complaints it receives, how many it investigates, and,
22 you know, what actions it takes in turn, and as well as
23 a number of multiple complaints filed against specific
24 preparers or firms, which makes it difficult to
25 identify causes of problems and areas of non-

1 compliance.

2 So, in addition to improved guidance and
3 standards, we think it would be important for the IRS
4 to consider consolidating or centralizing the
5 oversight.

6 That concludes my statement, and I look
7 forward to any questions you have.

8 MS. HAWKINS: Great. Thanks so much, Mike.
9 Next up is Celeste Heritage who, for the last 13 years,
10 has been the Administrator of the CTEC Program in
11 California and I know she's seen it all from soup to
12 nuts at this point. So we're looking forward to
13 hearing from you.

14 California Tax Education Council (CTEC)

15 MS. HERITAGE: Thank you. Again, my name is
16 Celeste Heritage. I'm a Vice President with
17 Advocation, Incorporated. We're a legislative advocacy
18 association management firm based in Sacramento,
19 California, and I'm here on behalf of the California
20 Tax Education Council, CTEC.

21 Our firm has administered the CTEC Program
22 for the last 13 years. I'd like to thank the IRS for
23 the opportunity to be here and share our views and
24 experiences regarding the CTEC Program.

25 In 1997, a law was passed in California which

1 transferred the responsibility for approving tax
2 schools and certifying the education of tax preparers
3 from the Tax Preparer Program which was administered by
4 the California Department of Consumer Affairs to CTEC.

5 CTEC is a non-profit corporation. It
6 regulates any person who, for a fee, assists with or
7 prepares tax returns for another person. CPAs who are
8 licensed by the California Board of Accountancy, EAs,
9 attorneys who are active members of the State Bar of
10 California and their employees are all exempt from the
11 tax preparer law.

12 At the time of the transfer, there were
13 approximately 27,000 registered preparers in the state.
14 Each year, our registration numbers have increased to
15 the point where we currently have over 44,000
16 registered preparers.

17 CTEC-registered tax preparers, CRTPs, are
18 required to take an initial 60 hours of education from
19 a CTEC-approved provider and 20 hours of continuing
20 education annually to remain in compliance. CRTPs are
21 also required to carry a \$5,000 tax preparer surety
22 bond.

23 CTEC not only registers preparers, it also
24 approves tax education schools. These schools go
25 through an extensive review process by staff as well as

1 a thorough curriculum review by individuals with a tax
2 education background.

3 Every three years, an approved provider is
4 required to have their materials re-reviewed.

5 Currently, CTEC has approximately a 125 approved
6 schools.

7 In order to register with CTEC, an individual
8 is not required to take a standardized test. However,
9 education providers are required to administer a final
10 examination for all students taking the 60-hour course
11 by distance learning. That would be your
12 correspondence courses, your interactive courses.

13 Although most providers do administer a final
14 examination for instructor-led classroom courses, such
15 exams are not currently mandatory but will be in 2010.
16 This same procedure could be used for a national
17 registration program. Rather than a standardized test
18 taken at testing centers, individuals could be required
19 to take a final exam given by the education provider.
20 This exam could be a standardized test, various
21 versions, developed by the IRS and given to providers
22 for their use.

23 In considering a national program, the
24 imposition of an upfront entrance exam could cause
25 serious harm to the livelihoods of those preparers

1 unable to pass the exam. Some individuals simply are
2 not good test-takers. CTEC believes it would be better
3 to initially register all unlicensed preparers, collect
4 the registration fees to fund the program, and impose
5 an annual continuing education requirement on all
6 registrants.

7 This is with the expectation that after a
8 year or two, these individuals would be required to
9 take and pass a standardized test to retain their
10 registration. This approach would be less likely to
11 drive preparers underground and get most on the radar
12 screen upfront.

13 There is also some concern that a federal
14 program might follow Circular 230 and limit CPE to
15 federal tax issues only. CTEC believes it is essential
16 that California tax preparers have education in the tax
17 laws of California and that this requirement should be
18 part of a federal program.

19 Since its inception in 1997, no government
20 money has ever been spent on the administration of the
21 CTEC Program. It is entirely funded from the annual
22 registration fees which are currently \$25. There is a
23 late fee of \$13 if an individual registers late.
24 Rather than paying the 25, they would pay 38.

25 There is a fee to providers for the

1 curriculum review that's either \$500 or \$1,000, plus
2 CTEC sells merchandise. We have mailing lists we sell,
3 brochures, posters. These fees are used primarily to
4 fund administration, review of provider curriculum,
5 enforcement, and public awareness.

6 Essential to the success of the CTEC Program
7 has been the development of a state of the art computer
8 system. During the 2008-2009 registration cycle, over
9 30,000 preparers registered online. Unlike the manual
10 random auditing of selected CPAs and EAs, CTEC verifies
11 the education of every preparer prior to their initial
12 registration and before their renewal is complete.

13 This is accomplished by mandatory online tax
14 school reporting. Each approved provider is required
15 to verify electronically their student's education with
16 CTEC. To assist providers with this process, a bar
17 code procedure was developed whereby each preparer
18 receives an ID card with a bar code on it.

19 This bar code then can be scanned at the time
20 of the class and used by the provider to simplify the
21 electronic sending of information. The system also
22 allows preparers to view their educational records and
23 find schools where they can take their education.

24 Due to this automation, Advocation is able to
25 administer the program with the staff of only three

1 full-time people.

2 One of the most important responsibilities
3 undertaken by CTEC is to educate California taxpayers
4 on the selection process of a tax professional. Most
5 years, between a \$150 and \$200,000 of the CTEC budget
6 is allocated for paid advertising throughout the state.
7 Thousands of dollars in free advertising, PSAs, media
8 interviews, are also utilized to get the message out.
9 Brochures, posters, and attendance at all tax events
10 help convey to the public the importance of selecting a
11 registered tax preparer.

12 The key to any law is enforcement. For this
13 reason, CTEC for the last six years has partnered with
14 the California Franchise Tax Board to provide the
15 needed enforcement arm of the program. Currently, CTEC
16 budgets \$350,000 annually to FTB for this service.

17 In return, FTB Fraud Unit investigators are
18 out in the field identifying and fining illegal
19 preparers.

20 Finally, a question that is frequently asked:
21 because of the Tax Preparer Act and the regulations
22 imposed on tax preparers, are tax returns prepared more
23 accurately in California than in states that do not
24 have such laws?

25 We have looked for statistical data that

1 could be used to validate whether any group of
2 preparers does a better job of preparation than
3 another. Unfortunately, it would appear that there is
4 no data publicly available. Thus, it seems completely
5 illogical that a tax preparer who has no education at
6 all would be a better option for California consumers
7 than a preparer who has completed 60 hours of
8 qualifying education and maintains 20 hours of
9 continuing education annually.

10 MS. HAWKINS: Thanks very much, Celeste. Our
11 next speaker is Ruth Moore. Ruth is with the Franchise
12 Tax Board. She has both a CPA and is a Certified Fraud
13 Examiner. So she's eminently qualified to talk to us
14 about what the FTB does with its preparers.

15 California Franchise Tax Board

16 MS. MOORE: Well, thank you for inviting us
17 on this very important issue.

18 The Franchise Tax Board's role in the
19 regulation of tax preparers is very unique. FTB does
20 not regulate the tax preparers. Attorneys are licensed
21 under the California State Bar. The California CPAs
22 are certified by the California Board of Accountancy,
23 enrolled agents by the IRS, and CRTPs, CTEC-registered
24 tax preparers are registered by CTEC.

25 Each of these bodies set their own

1 requirements for their members to earn the designation
2 that allows them to prepare tax returns. California
3 has approximately around 80,000 different tax
4 preparers, so we have a very large group of people
5 preparing taxes.

6 FTB's role is the enforcement arm for CTEC.
7 We were authorized by legislation to enter into an
8 agreement with CTEC to carry out their enforcement
9 efforts. As part of this agreement, CTEC agrees to
10 reimburse the Franchise Tax Board for any expenses
11 incurred to implement their efforts.

12 The enforcement effort is for registration
13 only. We are not in the process of looking at the
14 quality of the returns, though we are as a Franchise
15 Tax Board very much interested in getting quality
16 returns.

17 California Revenue and Taxation Codes,
18 Section 19.167, provides for a \$2,500 penalty for non-
19 exempt unregistered tax preparers who prepare personal
20 income tax returns for a fee. If, after notification
21 and the 90-day period, the preparer does not become
22 registered and continues preparing tax returns for a
23 fee, the penalty is issued.

24 If the preparer continues to prepare returns
25 without becoming registered, the penalty becomes \$5,000

1 for each subsequent period of non-registration. Last
2 year, we issued around 320 penalties and 72 of those
3 were -- 72 percent of those did become registered
4 within the 90 days. So we have a good compliance
5 record once they're notified.

6 FTB's effort, first and foremost, is an
7 effort at bringing the tax preparers into compliance.
8 We educate the preparers about the -- the ones who are
9 unregistered about CTEC and their responsibilities as
10 tax preparers, both to their clients and to the taxing
11 agencies.

12 We work with these unregistered people to
13 become knowledgeable about CTEC and the requirements to
14 become registered. We teach them to use CTEC's
15 websites for identifying education providers and what
16 the rules and regulations are. We share with them the
17 required dates to become registered and answer
18 questions, both at the time of the visits and during
19 the 90-day period.

20 Only upon the tax preparer's failure to
21 become registered within the 90 days do we issue the
22 \$2,500 penalty. The confirmation that the taxpayer
23 compliance is in compliance with the registration comes
24 from CTEC. We can see from CTEC's online database that
25 the preparer has registered and the date that they

1 became registered, so we can determine if it's within
2 the 90 days or not. If it's within the 90 days, we
3 remove the penalty. If not, the penalty stands. The
4 penalty can be appealed. They have to pay what they
5 owe and then file an appeal.

6 Some of the challenges that we face in doing
7 this is the one that was mentioned. It's not easy for
8 us to find out who prepares what group, what regulatory
9 obligation group they belong to, and having a variety
10 of members makes our process incredibly difficult.

11 Since tax preparers can sign the return with
12 their social number, the preparer identification
13 number, and FEINs, that is many different ways for us
14 to try to find out who they are and that's only looking
15 at the people who actually sign the return
16 appropriately. We find many preparers who put in any
17 kind of number just so it completes that field.

18 So when we get an SSN, we can then look to
19 identify who the preparer is on our tax system as an
20 individual, but for that, we then have to go to three
21 other databases to identify what kind of a preparer are
22 they? Are they a CPA? Are they an attorney or are
23 they a CRTP?

24 We have real problems with the EAs because
25 the information we get from the IRS is name and address

1 only, no social security numbers. So it makes it very
2 difficult for us to find out who the EAs are from when
3 we're matching to all those preparers that have
4 prepared returns to who they are associated with.

5 So we all -- how we get around that is we
6 work with the California Society of CPAs -- or EAs and
7 they share their risk but that only covers about half
8 of the EAs.

9 If providers are using the PTIN, then we have
10 to go to our PTIN database first, get the social
11 security number and then go back to all the other
12 databases to identify who the preparer is. The fee
13 makes it even more difficult because that's a one-to-
14 many ratio. So we really don't even know who is
15 preparing the return when they're using their federal
16 employment identification number and from our
17 experience, 20 to 30 percent of those searches result
18 in numbers that are not valid.

19 As a result, we end up contacting many
20 taxpayers who've met their legal obligation in order to
21 find the unregistered and at the same time we miss many
22 preparers who should be registered but we're not aware
23 of because we can't identify them using our current
24 system.

25 Another issue is CTEC does not have the

1 ability at this time to remove a tax preparer from
2 being registered with them. They are limited by their
3 enabling legislation to do so. They are currently
4 working on getting that law changed so that we can do
5 it, but what happens is if you have a preparer who's no
6 longer allowed to be, say, a CPA or an attorney or EA
7 but they're still preparing returns, that preparer must
8 then get registered with CTEC or they'll get the
9 unregistration penalty.

10 So this process takes those preparers with
11 issues and pushes them down to clients with less skills
12 in determining if they're a good preparer or not. For
13 an example, if you have a preparer who's removed by
14 Accountancy for embezzling from their clients, if they
15 -- CTEC has no provision for excluding them for
16 registration and preparing returns, but this is also
17 true with the IRS.

18 The IRS can prevent a tax preparer from
19 representing clients before the IRS, but it does not
20 prevent them from filing tax returns, and the issue is
21 when you have a bad preparer, and we all agree there
22 are some, they need to not be filing returns.

23 And the problem that California has, if we
24 choose to exclude them on our own, then you either run
25 into they go underground or how do we handle the issue

1 we tell them they can't provide a California return but
2 they still prepare federal returns and so now we have
3 the client, the taxpayer, saying, well, now I have to
4 go somewhere else to get my California return prepared.
5 So our concerns are that in those cases, we'd get fewer
6 returns. So that really is a big issue.

7 The protection that taxpayers need is having
8 tax preparers who are educated in tax laws who will
9 provide accurate returns and will charge the clients a
10 fair fee for their services and we all know that there
11 are some preparers that should not be preparing
12 returns.

13 The other issue we run into is the number of
14 tax preparers who are not filing their own returns. We
15 took the entire CTEC database, ran it against our tax
16 filing system, and found around 25 percent of those
17 aren't doing their own tax returns.

18 So our recommendations are that California
19 really supports the idea of one identifying number to
20 use in signing a return. The single number would make
21 the process of identifying who the tax preparers are
22 much more efficient and accurate. The identifying
23 number needs to identify the professional designation,
24 the taxpayer's name and other identifying information,
25 requiring the social security number, as well as their

1 address, phone number.

2 To make this number more effective, the
3 identifying number must be used for both federal and
4 state returns, and that number, along with all the
5 associated information, must be shared with the states
6 for their use. That way we can work together to
7 identify who the bad preparers are or the preparers
8 with problems, and as stated, we can't even identify
9 the preparers to be able to look at them to see who
10 makes what kind of mistakes, who does a good job,
11 because if we had that information, we could really
12 work with the different groups and bring about the
13 education they need to help them do a better job.

14 The IRS and states need to work together to
15 ensure the tax preparers meet their regulatory
16 obligations. Enforcement is a necessity. And we must
17 also work together to educate taxpayers to choose good
18 preparers.

19 As part of my fraud work, we will see some
20 people using a bad preparer, we'll notify them through
21 disallowing whatever the credits are, but then they'll
22 turn around and go to another bad preparer.

23 So the Franchise Tax Board has a Tax Gap
24 Strategic Plan and one of the goals is supporting the
25 high standards of tax professionals. Our compliance

1 efforts with CTEC we see as contributing to meeting
2 this goal. One of the things we also do for CTEC is
3 that any time we do any publications or any kinds of
4 news events about the different preparers, we include
5 the CRTPs in that discussion.

6 The FTB supports the effort to help educate
7 tax professionals to prepare quality returns. CRTPs
8 initially must complete 60 hours of tax preparation
9 training prior to preparing returns for a fee. In
10 addition, they must complete 20 hours of continuing
11 education to remain a CRTP and it has to in both
12 federal and state tax training.

13 FTB believes that this training contributes
14 to more knowledgeable tax preparers than those without
15 any education.

16 Thank you.

17 MS. HAWKINS: Thank you, Ruth, and I'm happy
18 to hear some of your observations so that we can learn
19 from the mistakes that California already recognizes
20 that it has run across.

21 Our next speaker is Wallace Eddleman. Mr.
22 Eddleman is with the State of Maryland in their Revenue
23 Administration Division. Maryland has a law in the
24 process of implementation. So we're anxious to hear
25 what you have planned.

1 registration requirement and they do have a page on
2 their website. You can visit that and you can register
3 to stay tuned for any additional information that they
4 have as they get the program off the board -- off the
5 ground.

6 The Comptroller is very supportive of this
7 and wants to do everything that he can to help move
8 this forward and has volunteered his staff to assist in
9 any way they can to help get this off the ground.

10 It provides for licensure without examination
11 to someone if they've got 15 consecutive years of tax
12 preparation service. So there's a grandfather clause
13 there. It provides for licensure by examination, as
14 well, and that exam, for those who don't have at least
15 15 years' experience, can be no less stringent than the
16 individuals section of the special enrollment
17 examination for enrolled agents.

18 Licenses will have to be renewed every two
19 years and they will be subject to -- the renewals will
20 be subject to 16 hours of continuing education, eight
21 hours annually.

22 Our legislation also provided that there are
23 certain individuals that would be exempted from this
24 registration requirement and that would be a CPA
25 license in Maryland or any other state, an individual

1 admitted to the practice of law in Maryland or any
2 other state, an individual employed by a local, state,
3 or Federal Government but only in the capacity of their
4 official duties, they're doing tax-related work, and an
5 individual enrolled to practice before the IRS under
6 Circular 230, and then, finally, an employee or an
7 assistant of a licensed individual tax preparer or any
8 exempted individuals in the performance of official
9 duties in the capacity of or on behalf of their
10 employer.

11 The bill also provides that the Board will be
12 adopting Rules of Professional Conduct to ensure a high
13 standard of practice of individual tax preparation.
14 They will also be responsible for maintaining records
15 of complaints regarding individual tax preparers in
16 Maryland. That's something that we don't have right
17 now. We don't -- although we get a lot of complaints,
18 I don't have any statistical information from Maryland
19 of, you know, what we're dealing with. We just know we
20 have it and we have a lot of it.

21 The Board will also be authorized to deny
22 registration, reprimand registered individuals, or
23 suspend or revoke a registration for fraudulently
24 obtaining or using a registration, engaging in criminal
25 activity, or engaging in professional misconduct in

1 accordance with the Rules of Conduct that they
2 developed.

3 They'll be able to impose penalties, as well,
4 up to \$5,000 for each violation. The practitioner or
5 the tax preparer would have the right to have an appeal
6 hearing before the Board, before the Board took any
7 kind of final reprimand or penalty action, and then if
8 the penalty or the reprimand is imposed by the Board,
9 that tax preparer would have appeal rights to the
10 Office of Administrative Hearings in Maryland.

11 Persons aggrieved by an individual tax
12 preparer under this Act could also be able to sue for
13 civil damages under the Act.

14 The Act also provides that a violation of the
15 Act is an unfair or deceptive trade practice under the
16 Maryland Consumer Protection Act and also subject to
17 the MCPA Civil and Criminal Penalties, as well.

18 But like I said, unfortunately,
19 notwithstanding the June 1, 2010, effective date for
20 the licensing, the implementation is contingent on the
21 appointment of a board which hasn't happened yet, as
22 well. I understand that there is some efforts being
23 made to get that moving and then also the appropriation
24 of funds by the Governor's Office.

25 As I said, the Comptroller was a strong

1 supporter of this legislation, the Maryland Cash
2 Campaign and many others, and the Comptroller testified
3 on behalf of this legislation and why it was so
4 important and why we still believe it's important to
5 get this off the ground as soon as possible.

6 The Comptroller's Office receives more than
7 1.3 million tax returns from paid preparers each year
8 and it's safe for us to bet that a majority of the tax
9 preparers the taxpayers believed they were using
10 qualified, certified, or registered professionals and
11 that's not always the case, as we see daily.

12 While Maryland tax attorneys, CPAs, and
13 enrolled agents who are exempt under this licensure,
14 they are subject to other ethical standards and their
15 own boards and the like, there are many people
16 advertising them out themselves as, you know, tax
17 preparers or, you know, specialized tax preparers and
18 kind of giving themselves the same type of credentials
19 that maybe the CPAs or attorneys would be having when
20 they don't really have any types of credentials at all.

21 In the past and currently, since the Act has
22 not been funded, anyone can call themselves a tax
23 preparer in Maryland, whether they're qualified or not,
24 and they're not subject to any type of scrutiny, and in
25 many cases they're not qualified.

1 The Comptroller's Office sees the problems
2 that results from returns prepared by individuals who
3 are at best uneducated in the tax area and at worst
4 intentionally deceiving people and earlier in my
5 career, I was a hearing officer for the Comptroller's
6 Office hearing contested tax appeal cases and I saw
7 firsthand taxpayers come in on audit when their return
8 was detected by our Questionable Returns Unit and they
9 were assessed and deductions were disallowed. They
10 would come in to the hearing on audit and just be --
11 had no idea that they had claimed, you know, employee
12 business expenses and home office deductions on their
13 return. They just had no idea.

14 They signed the return but, you know, they
15 had no idea and, unfortunately, a lot of times had no
16 idea who prepared their return. So they were really in
17 a rock and a hard place, and the preparer kept all
18 their documentation. So they really -- it really is
19 bad and we just see it way too often.

20 And in addition, in many instances these
21 taxpayers are promised large refunds when these
22 preparers fraudulently complete their return because
23 these preparers are going to, you know, do a tax refund
24 loan to them, charge them exorbitant rates of interest,
25 taxpayer then owes the loan and the high interest rate,

1 and then gets audited and owes the tax refund back. So
2 it's really predatory behavior. It's a great concern
3 to the Comptroller of Maryland and we believe that this
4 Maryland Tax Preparers Act, although not going forward
5 yet, is a big step in the right direction.

6 This is a pro-consumer measure that helps
7 protect the taxpayers against unscrupulous tax
8 preparers. It also gives the state a method of
9 tracking preparers which we are not doing now. The
10 Board is charged with keeping track of all the
11 complaints that are filed and the discipline taken
12 against these individuals so they can be identified and
13 I know we have a few lists of tax preparers that, you
14 know, we just see the same name coming up that we can
15 identify and like California, we are also looking at
16 some of the tax preparers to see if they filed their
17 own returns and we're, you know, running jobs that we
18 can identify if they put their identification number on
19 there, the preparer, if we can all identify all the
20 returns that this preparer has prepared, and then start
21 looking at all of those returns, and we are trying to
22 take steps like that.

23 Again, the legislation provides for an eight-
24 person regulatory board which is to provide a mechanism
25 for ensuring that individuals holding themselves out as

1 tax preparers have the requisite knowledge to prepare a
2 basic return.

3 MS. HAWKINS: Well, I think much of the rest
4 of your comments are probably contained in your written
5 materials?

6 MR. EDDLEMAN: Yes.

7 MS. HAWKINS: I don't want to short-change
8 Jamie and Ron. Thank you very much.

9 MR. EDDLEMAN: Thank you.

10 MS. HAWKINS: The next speaker is Jamie
11 Woodward. Jamie is Acting Commissioner in the State of
12 New York and has, as Wallie, the formidable task of
13 overseeing the implementation of a law that has yet to
14 be put in place.

15 New York

16 MS. WOODWARD: Thank you, Karen, and thank
17 you for the opportunity to appear before you today.

18 First, I want to express the support and
19 enthusiasm that I and my colleagues in both Tax
20 Administration and Consumer Protection in New York have
21 as the IRS takes steps to secure long overdue
22 regulation of the tax return preparer industry.

23 In recent years, we in New York observed that
24 the tax preparation field was fast becoming a lucrative
25 market for unscrupulous individuals, many with

1 absolutely no background or experience in taxation.
2 Anyone in New York, regardless of education,
3 experience, training or even criminal history, can call
4 themselves a preparer and charge the public for
5 services they provide.

6 Nearly 60 percent of New York personal income
7 tax returns are prepared with the assistance of someone
8 who is paid for that service. These preparers are
9 uniquely situated to influence taxpayer behavior and
10 become a powerful force behind the taxpayer's decisions
11 to voluntarily comply with the tax law or, conversely,
12 to commit tax fraud or other criminal acts, yet there
13 are no New York State or national standards under which
14 these individuals and businesses operate.

15 In New York, we are in the first stages of
16 developing minimum qualifications and standards for
17 this industry and we look forward to working with our
18 colleagues at the IRS to effect meaningful change.

19 Just this past year, Governor Patterson and
20 our legislature directed my department to begin to
21 register tax preparers who are not otherwise regulated
22 as licensed accountants or attorneys.

23 The legislation also directs the Tax
24 Commissioner to chair a task force of government and
25 industry representatives, including the IRS, and to

1 make recommendations for minimum education and
2 licensing standards for all tax preparers operating in
3 New York. We're actively organizing this task force
4 now and it certainly works that we're working with the
5 IRS on this matter, as well.

6 In response to what appears to be a growing
7 culture of creative tax avoidance fueled by
8 unscrupulous tax preparers, our department in recent
9 years has devoted significant resources to
10 investigating and prosecuting those preparers. To get
11 a clear view of the extent of the problem, we borrowed
12 investigative techniques more commonly used in rackets
13 investigations. We went undercover.

14 In less than two years, we conducted nearly
15 200 covert operations in which our agents posed as
16 taxpayers seeking to hire tax professionals to prepare
17 income or sales tax returns. While our selection of
18 preparers would not be considered random in the
19 scientific sense, we did attempt to select preparers
20 from across a broad spectrum of the community.

21 Our findings revealed an epidemic of
22 unethical and criminal behavior by these tax preparers.
23 In the 20 months since we began this project, we've
24 arrested more than 20 preparers and secured 13
25 convictions. Of course, our investigations are

1 continuing and additional arrests are anticipated.

2 Our investigations uncovered fraud by
3 preparers of all types, from storefront operations to
4 licensed professional CPAs. All used their knowledge
5 of the Tax Administration to operate as fraud coaches
6 and help our undercover agents cheat without getting
7 caught.

8 There was nothing subtle about these
9 preparers' sales pitch or their instructions. One told
10 us he was going to give us an education as to how to
11 hide our money without getting caught. Another said he
12 specialized in preparing plain vanilla tax returns
13 where taxpayers can cheat without triggering an audit.

14 Many of them told us we wouldn't get caught
15 if we didn't file and when we decided to file anyway,
16 they coached us to evade taxes by hiding or destroying
17 our business records, creating new or false records, or
18 by hiding our cash, lying about our income, or
19 inflating and creating expenses.

20 These return preparers created -- fully
21 reflected their willingness to cheat and encouraged
22 others, actual strangers, to cheat. All appeared to
23 promote the concept that a calculated risk to cheating
24 was low and full compliance was optional.

25 One preparer suggested we could get away with

1 reporting only one-tenth of our income. Another, a
2 CPA, gave us a choice of paying 25 percent of the tax
3 we owed, 50 percent, 75 percent, or the full amount.

4 (Laughter.)

5 MS. WOODWARD: One joked that he would use
6 his magic pencil to create a false return and several
7 preparers told us that we could get away with reporting
8 only our credit card sales and not report any cash
9 transactions on sales tax returns.

10 In addition to investigating preparers who
11 are fraud coaches, we were also investigating tax
12 preparers who want to facilitate refund mills. These
13 operations create and file thousands of fictional tax
14 returns each year, often taking advantage of the less-
15 educated, unsuspecting taxpayers and putting them at
16 risk.

17 Our investigators, working with the IRS, have
18 uncovered preparers who sell dependents, create or
19 steal identities, and then forge documents to escape
20 detection on audit.

21 Through the use of predictive modeling and
22 other audit selection tools, we have been able to
23 identify questionable preparers whose returns we
24 monitor very closely. Not only has this saved New York
25 taxpayers hundreds of millions of dollars in fraudulent

1 refunds we deny, but it has also helped us initiate
2 criminal investigations and to prosecute the
3 unscrupulous preparers.

4 New York recognizes the need to bring
5 oversight to the preparer industry and, as I mentioned,
6 we are starting a registration process for income tax
7 preparers for this upcoming tax season. We will be
8 issuing a registration ID for each preparer.

9 Understanding the states' perspectives and
10 providing a national structure of normal requirements
11 will go a long way to protect both state and federal
12 revenues as well as the taxpaying public. It will also
13 head off any potential patchwork that could result if
14 states seek individual solutions.

15 All consumers across the country, consumers
16 who seek to comply with state and federal tax laws,
17 deserve the knowledge that our tax preparers are
18 trained and educated in their field.

19 As to our specific suggestions regarding the
20 development of a national program to regulate the
21 preparer community, I offer the following.

22 First, we strongly suggest that the IRS
23 register all tax preparers, including the CPAs and
24 attorneys. Each preparer should be given a unique
25 number people have talked about and important

1 registration information should be public.

2 Further, the IRS should promote data matching
3 and information sharing with and between the states
4 regarding investigations or concerns regarding
5 incompetent or unscrupulous preparers.

6 Minimum competency standards should be
7 developed and thought given to the requiring continuing
8 education.

9 Consideration should also be given to
10 regulating the terms of refund anticipation loans
11 through the regulation of the preparers themselves.

12 Finally, perhaps the most difficult, a public
13 education campaign as to the importance of dealing with
14 a reputable preparer is essential. Whether through
15 enforcement actions or cooperation in creating much-
16 needed regulatory schemes, New York stands ready to
17 work with the Federal Government to achieve meaningful
18 oversight of the tax preparation industry.

19 Thank you.

20 MS. HAWKINS: Thanks very much, Jamie, for
21 those thoughtful comments.

22 Our last speaker is Ron Wagner, the Executive
23 Director for the Oregon State Board of Tax
24 Practitioners, and the person here who has the most
25 experience, at least in the state, that has the most

1 experience in regulating paid tax preparers. So we're
2 very interested to hear what you have to tell us.

3 Oregon

4 MR. WAGNER: Great. Well, thank you very
5 much, both for the opportunity to be here and to share
6 with all of you Oregon's story.

7 In Oregon, it's really all about protecting
8 consumers. We are a consumer protection agency and we
9 take that very seriously.

10 Interesting that Oregon has been in -- the
11 Oregon Board of Tax Practitioners has actually been in
12 existence for 36 tax seasons. Thirty-seven years ago,
13 a group of practitioners went to the legislature and
14 asked to be regulated, a pretty unusual step for folks
15 to take to want to be regulated, but they really wanted
16 to see the industry cleaned up in Oregon and to create
17 a profession. So in 1972, that group did that, or '73,
18 and it began in '74 tax season.

19 Who do we regulate? We regulate, like some
20 of these other groups, anyone who prepares, advises or
21 assists in the preparation of a tax return for a fee in
22 Oregon, can be a federal return or an Oregon return,
23 who is not a CPA or an attorney or someone who works
24 for a CPA or attorney or someone who works for a
25 corporation and prepares that corporate return.

1 We do regulate enrolled agents in the state
2 of Oregon.

3 Our licensing requirements are quite
4 stringent. We require an 80-hour -- completion of an
5 80-hour basic tax course in order to sit for the
6 preparer exam. We have two levels of licensure. We
7 have an entry level which allows someone to prepare
8 returns in Oregon under the supervision of a more
9 experienced higher-level licensee.

10 They're required to have at least 780 hours
11 of tax preparation in two of the prior five years in
12 order to qualify to take the higher-level license exam
13 which is for the licensed tax consultant. Those who
14 take the licensed tax consultant exam and pass that
15 then are able to work independently without any
16 supervision.

17 We think the model of the two levels of
18 licensure works very, very well, answers our taxpayers
19 very well.

20 Our ongoing qualifications. We require all
21 of our licensees, whether they are licensed tax
22 practitioners or licensed tax consultants, to obtain a
23 minimum of 30 hours of continuing education each year.
24 The average number of hours that our licensees obtain
25 each year is actually closer to 40 hours. It's about

1 30 hours of education each year. Some of our licensees
2 receive a 100 hours, some even 200 hours during a year.

3 They maintain professional standards and
4 state ethics. They are required to file a license
5 renewal form and pay the appropriate fees each year.

6 I've actually been in the job just a year and
7 a half now, so it's new to me which in some ways is
8 very good. I've looked at the Board to see what have
9 they done right. A few things I think they've done
10 right is, Number 1, created two levels of licensure.

11 For someone who has never been involved in
12 the tax preparation industry to come in, they're coming
13 into the industry. They've worked under the tutelage,
14 under the supervision of someone more experienced and
15 what it has done it has created really a mentorship
16 program. We think that that has served our consumers
17 extremely well.

18 When our program began 36 years ago, we did
19 allow grandfathering. We think that worked well. The
20 Board is currently self-supporting. We do receive
21 absolutely no general fund dollars. We're funded 100
22 percent by licensee fees and the funds that are
23 collected through our compliance efforts.

24 Regulation at the local level, just like
25 CPAs, are licensed and regulated by the State Board of

1 Accountancy. Attorneys are regulated by their groups
2 in their states. Regulation at the state level has
3 worked very, very well in Oregon and again we think
4 serves as a very good model nationally.

5 Last, we took action. I've asked myself
6 questions and I have been there really just a short
7 period of time and said this Board started 36 years
8 ago. What would we do differently if we were putting
9 this Board together today? Very surprisingly, I've
10 come up with a very, very small list. I'm very
11 impressed with those who went before me 36 years ago.
12 I think they had incredible insight and did most things
13 very well.

14 But with that said, what would I do
15 differently? I'd probably require a specific number of
16 continuing education hours which are required each year
17 to be on tax law updates. Currently, there are a
18 minimum of 30 hours of education. It can be anywhere
19 within the approved group of classes. There's no
20 requirement that any specific number must be related to
21 new law update and I think that is absolutely critical.

22 We did a lot of grandfathering. I think that
23 worked fairly well. I'm not sure today I would allow
24 grandfathering but require all tax practitioners should
25 show competency of tax law.

1 We know we've all had stories of people who
2 have prepared tax returns for five years, 10 years.
3 The length of preparing tax returns does not
4 necessarily coincide with one's competency or knowledge
5 of tax law. So I say come to Oregon, prove that you're
6 competent with tax law.

7 The last item would be include more
8 sophisticated returns. Clearly, Oregon's licensing
9 requirements only relates to the appropriation of
10 personal income tax returns. So those who prepare
11 corporate return, a partnership return, trust or estate
12 do not fall under the jurisdiction of the Board in
13 Oregon.

14 We did have legislation that we took to the
15 Oregon legislature this session earlier this year. The
16 legislation passed through the Senate, got caught up in
17 the House side and, unfortunately, did not become law,
18 but we will certainly continue those efforts in our
19 next legislative session.

20 I've attended the IRS Tax Forums the last two
21 years after I became the director and have had some
22 very interesting conversations. One gentleman came up
23 to my table a year and a half ago and he was driving
24 through rural Texas. He said he came upon a business
25 and it said Automotive Repair, Texas Barbecue and

1 Taxes.

2 (Laughter.)

3 MR. WAGNER: That's a very interesting mix of
4 business, certainly not here to say the gentleman was
5 not competent. For all I know, he may have been
6 extremely competent. In Oregon, we want you to show us
7 that you are and we demand you do show.

8 This year, at my table I had numerous people
9 come by. One of the comments I remember is someone
10 looked and said, "Oh, you're from Oregon. Oh, you're
11 the really difficult state." And actually, I enjoyed
12 the comment. I said, "Yes, we are. We demand high
13 competent levels and high ethics. Come to Oregon. You
14 can prepare returns, but come and we're going to put
15 you to the test."

16 In most states, as in Oregon, as I'm sure
17 most states, you have to have a license to cut hair.
18 You may snip in the wrong place. You may burn or frizz
19 someone's hair. You may be able to ruin their day.
20 Sadly, I've been on the end of that, had a bad haircut
21 in my time or two. Yeah. It may have ruined my day or
22 maybe my week until I get it fixed.

23 Tax preparers have the most confidential
24 personal intimate details of our lives. They have our
25 date of birth. They have our bank account records.

1 They have our family social security numbers. They
2 have all knowledge of our personal financial and family
3 history, yet they're not required in most states to
4 have a license. A licensed hair dresser can ruin your
5 day, a tax preparer can ruin your life.

6 In Oregon, we work hard to keep that from
7 occurring. We work to protect Oregon consumers.
8 That's the Oregon story.

9 Thank you.

10 Discussion

11 MS. HAWKINS: Ron, thank you very much, and
12 thank you all for your very insightful and helpful
13 comments as we go through our process, and I know that
14 the Commissioner has some questions for you.

15 COMMISSIONER SHULMAN: Yeah. Yeah. Thank
16 you. Those were incredibly thoughtful comments and
17 very helpful to us as we sort through these issues.

18 One of the things that several of you
19 mentioned was the issue of (a) exempting certain groups
20 that have other requirements, like CPAs, attorneys,
21 enrolled agents, and then (2) is the issue of
22 grandfathering.

23 Any time you're driving along the highway,
24 you've got a whole industry and then you're thinking
25 about raising standards, you've got to consider those.

1 We've had a bunch of commentators come to us
2 and say, you know, just because you're a CPA doesn't
3 mean you understand federal tax law and then we've had
4 commentators go the other way that say, you know, CPAs
5 have ethics that they can't do business, that they
6 don't understand and so that's part of that, and so I'd
7 like anyone who wants to comment on the thought process
8 that, especially the states went through when they
9 thought about exemption and they thought about
10 grandfathering because those are tricky issues for us.

11 MS. WOODWARD: I can start because in New
12 York, as we said, we just obtained legislation last
13 year and as a tax agency, we asked that it cover all
14 tax preparers because without knowing the universe of
15 who's doing it and having one system of numbering and
16 one -- just to say who's registered is Number 1.

17 Registering, whether you charge a fee or
18 whether you have the requirements for education or you
19 could, you know, make rules that the CPA, others, their
20 continuing education would cover what they were doing.
21 That's what we think our task force will look at, but
22 that you need to have the whole universe of who's
23 involved in preparing your tax returns.

24 Not all CPAs do taxes. Not all lawyers do.
25 Not all accountants do. So you're doing a lot of

1 sifting and looking through information. As I did note
2 in ours, we did not -- we were not successful at our
3 state level in encompassing all of those groups. The
4 legislature determined that we should not include the
5 CPAs and attorneys because they were registered
6 otherwise.

7 We, as tax administrators, think that will
8 become a hindrance to our ability to support the public
9 and to protect the public, but we will work with that,
10 but we would advocate that on the national level, that
11 a registration at least, minimal implication there,
12 registration and numbering system be covering everyone
13 who is going to do returns for pay.

14 COMMISSIONER SHULMAN: Thanks. Other
15 observations on this issue?

16 MR. EDDLEMAN: In Maryland, I would probably
17 say the same reason in that to get this legislation
18 passed and to get the support that was required,
19 probably we're going to need to exempt those already
20 licensed and registered individuals.

21 COMMISSIONER SHULMAN: Mr. Brostek, you had a
22 --

23 MR. BROSTEK: We don't have a particular
24 position on what should be done there, but a couple of
25 thoughts.

1 One, going back to this registration is
2 foundational, if you were not to include various groups
3 but you did require everyone to have a registered
4 identification number that they used, then you would be
5 able to see how well they performed and if it turns out
6 that they're not performing as well as one would like,
7 then you'd have the opportunity to reopen the issue
8 about whether to include them.

9 On the grandfathering issue, something that
10 always puzzles me here if someone has been practicing
11 for 10 or 15 or whatever years, I'm not going to assume
12 that they're fairly competent and I don't understand
13 why I would have a great deal of difficulty passing a
14 test, particularly if it's for the simpler tax returns.

15 One other thing on the grandfathering. If
16 you grandfather someone in, the taxpayer is going to
17 consider all people under your system to be qualified.
18 So you have to think also from the taxpayer's
19 perspective. If you don't actually have the same
20 confidence that the grandfathered people aren't going
21 to perform as well as others, then you've told the
22 taxpayer that they can have that confidence when you're
23 not really sure that they will.

24 COMMISSIONER SHULMAN: Both New York and, I
25 think, California talked about a public education

1 campaign, about using a certified preparer.

2 Do you have a database where people can check
3 to see who is registered and, if so, you know, what
4 issues are around -- came up around that?

5 MS. MOORE: Go ahead.

6 MS. HERITAGE: We have a database. All
7 44,000 of our registered preparers are on the database.
8 So an individual could go to our home page and click on
9 Verify Tax Preparer, put in a CTEC number if they know
10 one or put in a last name and that individual's
11 information, as far as their name and when -- you know,
12 if they're current is listed there, as well as their
13 address, I believe, and phone number. So it's very
14 helpful to people because a lot of people will call and
15 they're not sure.

16 For example, I'm not sure if the EAs have a
17 database. They were working on one to verify whether a
18 person -- we get a lot of calls and we always say if we
19 can't find them on our database, to please check the
20 Board of Accountancy in California or EAs.

21 COMMISSIONER SHULMAN: And so the argument
22 we've heard is that once you put a database in, you're
23 obviously giving people a seal of approval and, you
24 know, as you've all identified, there's going to be
25 people who register and you've got to have enforcement

1 and there's limited enforcement resources and so, you
2 know, that debate and so I'm curious your reaction to
3 those issues.

4 You have a minimal standard and everybody
5 gets on and gives a seal of approval potentially to
6 people who aren't as qualified or aren't going to give
7 as good of service as others.

8 MS. HERITAGE: And that's an issue and that's
9 one that we've now, because we've worked with TIGTA on
10 identifying some individuals, TIGTA has sent us
11 information on those people, paperwork, and we are
12 unable, due to our legislation, you know, due to the
13 law, to do anything about those individuals, but we
14 have gone back to the legislature.

15 We are currently working with them to get
16 language put into the law that we can get these people
17 off of our database, because basically what we're
18 telling consumers, it's okay to go to these people when
19 in fact it's not and that's been an issue for several
20 years and the California legislature is not -- it has a
21 difficult time taking the livelihood of an individual
22 away from them and so they're very reluctant to give us
23 that kind of language in the law.

24 COMMISSIONER SHULMAN: Yeah. Any other
25 comments?

1 MS. WOODWARD: Yes, we had similar concerns
2 in New York and what we came to for starters, the
3 program is just starting up, is to provide a
4 registration certificate that says that at this point,
5 it is not any endorsement of -- because we do not have
6 a testing standard. It's strictly a registration at
7 this time, but I also submit that not doing anything is
8 giving a seal of approval, as well, by having no
9 regulation and no system out there, we're by default
10 saying everyone's doing an okay job and that's no
11 better than moving on with a system that would
12 eventually allow us to control and register and examine
13 for competency.

14 COMMISSIONER SHULMAN: Ron?

15 MR. WAGNER: Oregon obviously feels very
16 strongly in an examination process which we use. Our
17 exams are 200 questions, 150 questions, all on federal
18 tax law, 50 questions on Oregon law and ethics. So
19 obviously we feel very strongly that people need to
20 show that they are competent.

21 We do have a licensee look-up on our website.
22 They can go and check. So they're seeing that someone
23 is competent. They have passed the minimum standard of
24 having passed either level of the exam. It shows that
25 they're currently licensed.

1 COMMISSIONER SHULMAN: Someone else?

2 MS. MOORE: It helps in California that the
3 taxpayers can at least go out and look and say if
4 someone's holding themselves out to be a CPA or a CRTP,
5 that they're on those look-up websites. We have a lot
6 of people who don't know about EAs because they don't
7 have that ability to do so, and we have a lot of
8 complaints about that.

9 So it also helps us when we're in the
10 enforcement to find out what category do these people
11 fall in and are they meeting their regulatory
12 obligations and without that it would make it much more
13 difficult for us to do the enforcement piece.

14 COMMISSIONER SHULMAN: We had a panel in late
15 July with some consumer groups and they posited to us
16 that one of the major problems with tax return
17 preparers was misaligned incentives and refund
18 anticipation products and some other refund products
19 that basically gave the preparer an incentive to jack
20 up a refund in order to get more money in their
21 pockets, sometimes hurting the taxpayer.

22 Ms. Woodward, you talked about looking at
23 refund anticipation loans, and I'm just interested in
24 people's views of that whole issue, what you've learned
25 over time as you've overseen this industry and any

1 insight you have for us around that issue.

2 MS. WOODWARD: Sure. Well, in New York, we
3 have approached that on a consumer protection level and
4 we have some required notices that the preparers need
5 to give to their clients. We would prefer to outlaw
6 those loans. We think they're predatory and they are
7 predatory and the high interest that goes along with
8 them.

9 Our problem on the state level is that we are
10 -- we have legal restrictions on what we can require
11 from banks and other national -- the whole legal end of
12 it. So we are trying to do it on an educational
13 process, but that's very difficult because you're
14 dealing with such a vast number of people who are on
15 the lower end of the educational spectrum often, but
16 also the people who everybody -- everybody wants
17 everything right away and in New York, we spend a
18 little more time reviewing our refunds before we hand
19 them out because of these issues with the fraudulent
20 preparation of refunds.

21 So it causes us quite a problem. We'd really
22 like to see a cooperative effort to approach that.

23 MS. MOORE: We have the same problem with
24 those loans. They generate most -- a great deal of our
25 fraud problems. We verify W-2s and withholding upfront

1 and many of those are directly fraudulent loans driven
2 by the refund anticipation loans.

3 We try to share that information with the IRS
4 and this year, in three and a half months, in
5 California, we sent over -- very close now to \$10
6 million of referrals of refunds that we know to be bad
7 from California, the W-2s were not valid, and we've
8 sent that information to our local IRS as quickly as we
9 discover it so that they can try to stop it, as well,
10 because our losses are minuscule compared to the
11 federal losses and so we've discovered in California,
12 even if we stop them, we've seen instances where the
13 preparers will not even file a California return.

14 You'll go in and look at the W-2, you'll see
15 that there's California withholding, they don't file
16 the California return. They'll say they'll do it
17 later. They file the federal for the earned income tax
18 credit and for the fraudulent withholding and that's
19 running into, we know for the IRS, millions of dollars.
20 So it's a big problem for us.

21 MR. BROSTEK: There certainly is work that
22 we've done that's shown that the refund anticipation
23 loans are used and that they're very high interest
24 rates on those loans.

25 In terms of dealing with them, part of the

1 problem is whether or not, as you imply, the person's
2 compensation structure takes into account how much
3 money they get back for the taxpayer. I'm not an
4 expert in the Circular 230, but I don't think that's an
5 allowable compensation scheme under 230.

6 MS. HAWKINS: There are prohibitions against
7 contingent fees which is really how that would be
8 measured.

9 MR. BROSTEK: So one way of thinking about it
10 for all paid preparers is it ought not to be a link to
11 compensation based on the amount of money that you're
12 giving the taxpayer back.

13 MR. MCKENNEY: I think some of the people on
14 the last panel had talked about the concerns about
15 having any type of a retail structure associated with
16 the tax preparation because it worked to provide an
17 incentive for them to get a higher refund than they
18 might be entitled to and that's true.

19 COMMISSIONER SHULMAN: All right. Let me
20 turn it over to Mark and Karen.

21 MR. ERNST: So, Mike, I want to go back to a
22 comment you made about sort of the accuracy correlation
23 between sort of studying different levels of accuracy
24 across different states and whether the Oregon
25 experience as an example, we can identify that there is

1 improved accuracy of returns coming from that state.

2 We don't know whether it's attributable to
3 the regulatory regime that exists there, but, you know,
4 certainly there would be a strong correlation.

5 I guess I'm interested in your -- everybody's
6 thoughts on how we should think about the cost-benefit
7 of some kind of a federal licensing regulatory
8 structure and how we can ensure that whatever that
9 structure is, it actually leads to improvements in
10 compliance, improvements in quality, as opposed to what
11 may or may not be the experience in some states where
12 there's registration but it doesn't necessarily --
13 hasn't proven necessarily to translate to improved
14 accuracy.

15 MR. BROSTEK: Well, a couple of facts on
16 cost-benefits. We tried to total up as best we could
17 the cost both to the states and to the practitioners of
18 the systems that the states have, particularly Oregon.

19 Normally when IRS does its cost-benefit, it's
20 looking at the federal cost only compared to any
21 revenue increase that would come in. We took into
22 account the entire cost and we didn't calculate exactly
23 where this might be beneficial, but overall the State
24 of Oregon had about \$390 million more in federal tax
25 payments because their returns are more accurate than

1 average in other states.

2 If 10 percent of that was due to the
3 regulatory regime, that's 39 million. The total costs
4 that we calculated for both the practitioners and the
5 state was around six million. Well, that would be a 6
6 to 7:1 return on investment. If you considered only
7 the 10 percent of the cost that was the state cost,
8 which is what you used for your calculation for cost-
9 benefit, the return would be much, much higher. So
10 it's one way to think about it. You need to try to
11 calculate the entire cost to the system.

12 In terms of deciding whether or not a system
13 is effective, you would have some advantages that we
14 didn't in the analysis we did. Again, a bit of a
15 theme. If you have a registration system and you can
16 have a baseline for the accuracy of the returns being
17 prepared, you have the ongoing NRP now, a learning
18 sample, so that you could get a baseline of what the
19 accuracy is, that could help you control for something
20 we couldn't control for.

21 We didn't know what portion of returns were
22 being prepared by CPAs or lawyers or enrolled agents,
23 who may have been more accurate than the unregulated
24 preparers. You could control for that if you did it
25 that way.

1 You also have the opportunity to do a before
2 and after analysis. We couldn't do that because the
3 two systems were enacted so long ago that there wasn't
4 data available. You would also be able to do a before
5 and after comparison.

6 MR. ERNST: And I think, Mike, you commented
7 that your work has shown that the changes that have
8 been made in the VITA testing process have led to
9 improvements in accuracy, at least in your state.

10 MR. MCKENNEY: And that's, I think, a fair
11 analogy, especially for the honest mistakes. Where
12 it's deliberate, I don't think it would have that kind
13 of effect.

14 But, you know, our sample that we did for
15 paid preparers, a lot of them were. They were just
16 people's misinterpretation of tax laws and
17 unfamiliarity with the tax laws. So I think that would
18 tend to follow a similar pattern for the honest
19 mistakes.

20 MS. HAWKINS: I'm sort of interested.
21 California and Oregon seem to have regimes that only
22 have enforcement associated with the registration
23 process. So maybe I just didn't -- we didn't give you
24 enough chance to tell me.

25 Do you have a way of going out after the bad

1 actors and taking them out of the system if there's
2 some of the kinds of egregious conduct that we were
3 hearing Jamie talk about?

4 MS. MOORE: Well, in California, when we find
5 some of the bad ones, we refer to our Investigations
6 Department and they can take it and get a criminal
7 conviction against them and then if that prohibits them
8 from filing returns, then we can implement that.

9 But the bigger concern for us is if we
10 prevent them from filing California returns but they
11 continue to do it for federal, they either go
12 underground or they do not file the California return
13 at all.

14 MS. HAWKINS: So the conduct either has to
15 rise to the level of something so egregious that it
16 warrants a criminal prosecution or they're in your
17 system, --

18 MS. MOORE: They're in our system.

19 MS. HAWKINS: -- unless we take them out
20 somehow?

21 MS. MOORE: Yes, we will -- I mean, we have
22 found them through doing some prepared audits that we
23 do, that by notifying all the clients that all of their
24 deductions or credits have been disallowed, it's a very
25 effective force against those preparers and it

1 literally changes their behavior.

2 We've had some with refundable credit that
3 we've disallowed 80 or 90 percent of what their claim
4 for their clients and then the next year they go from
5 preparing 800 returns down to maybe 70 returns with
6 those.

7 So we know that in those cases, when they
8 notice that we are paying attention, that it does have
9 a major effect, but you have to -- you have to enforce
10 the laws because they -- the questions we're going to
11 ask them would be, well, why are you doing this? Well,
12 nobody's checking. So if nobody's checking, we might
13 as well claim it.

14 MS. HAWKINS: Ron, how about you?

15 MR. WAGNER: In Oregon, we do -- we've had a
16 number of different levels. Number 1, we can keep
17 people out of the profession. We do have questions on
18 our applications. If someone has been disciplined in
19 another licensing agency or elsewhere, that may prevent
20 them from getting into the tax preparation industry in
21 Oregon.

22 So I think it was California maybe who made
23 -- somebody made the comment about, gee, you hate to
24 take away their livelihood, but again as a consumer
25 protection agency, we take that seriously and if you

1 have shown impropriety previously, it may prevent them
2 from their livelihood as a tax preparer.

3 So kind of off that from the get-go, the
4 baseline, we occasionally, it doesn't happen real
5 often, but we'll preclude someone from becoming
6 licensed. Once they're licensed with us, we do have a
7 pretty extensive group of laws that we can impose fines
8 on their activity, a minimum of \$50 up to a maximum of
9 \$5,000 per violation.

10 MS. HAWKINS: And this is for conduct as
11 opposed to just registration violations?

12 MR. WAGNER: Yes, correct, correct.

13 MS. HAWKINS: And it's just part of your
14 Civil Tax Code?

15 MR. WAGNER: That's correct.

16 MS. HAWKINS: Not unlike we have the preparer
17 penalty under the federal regime.

18 MR. WAGNER: Right. That's correct. The
19 Department of Revenue, we work more with kind of the
20 Code of Conduct of the tax practitioners as far as any
21 impropriety. As far as the filing of the return,
22 generally that is going to be handled more by the
23 Department of Revenue than by us.

24 MR. ERNST: But it sounds like once
25 somebody's in the system, it's hard for them to get out

1 or hard for your organization, your agency to deal with
2 them and remove them from their qualifications.

3 MR. WAGNER: At times it can be and probably
4 most often it can be. There are times when we do take
5 license -- the licenses away from the licensees.

6 MR. ERNST: And I was struck, Ms. Moore, by
7 your comment that said, you know, that 25 percent of
8 the CTEC registrants haven't filed their own returns
9 but presumably there's nothing you can do with that.

10 MS. MOORE: We're working on that. We're
11 working on that and putting that with our filing
12 enforcement program, so the information from the CTEC
13 database matches against what returns are filed with
14 California, and knowing that they did prepare returns,
15 we will then be able to do a filing enforcement on
16 them. So we're coming up -- this will probably be our
17 first year of doing that.

18 MS. HERITAGE: And it may be that that 25
19 percent is even higher because that's simply a question
20 on the application. Have you prepared your tax
21 returns? I mean, we're just asking them to check a
22 box, I mean, basically. So they could be telling us
23 the truth or not telling us the truth on that until we
24 go into the actual filings at the Board.

25 MR. BROSTEK: Okay. A couple of things on

1 enforcement to think about. There's an opportunity, as
2 I believe we heard in the states, for competitors to
3 have a self-interest in checking to see whether the
4 people who are preparing the returns are properly
5 licensed. You can have some self-policing in the
6 industry.

7 MS. HERITAGE: Absolutely.

8 MR. BROSTEK: You also do income tax audits
9 of one percent of the population every year. If part
10 of the income tax audit is determining whether a paid
11 preparer was used and then following up when a paid
12 preparer was not properly registered, that's another
13 part of the enforcement that could be done.

14 MS. HAWKINS: I think both Oregon and
15 California indicated that you not only -- if you have
16 an exempt individual, a CPA or an attorney or, I guess,
17 an enrolled agent in both of your states, who has
18 employees, they sort of get umbrella'd under that
19 person's exemption. Is that working?

20 MS. HERITAGE: That's correct, and just
21 recently now, FTB was finding when they were going out
22 to, for example, an office where there was an enrolled
23 agent, maybe that enrolled agent had several offices,
24 but he was only at the one but he had employees at the
25 other offices and in theory, the law, when it was

1 drafted, was that the enrolled -- the reason those
2 employees were exempt is because supposedly the
3 enrolled agent was overseeing the work, reviewing those
4 returns, signing those returns.

5 FTB found that that was not the case on their
6 visits. So we just now changed the law last year
7 where, if the enrolled agent is not reviewing -- only
8 the enrolled agent can sign the return. If, you know,
9 he has employees at another office, those employees
10 have to be registered with CTEC if he's not overseeing
11 the work and signing the return.

12 MS. MOORE: And that applies to attorneys and
13 CPAs, as well. I mean, I was going to say it gets to
14 the devil gets to the details and so when people say I
15 work for an exempt preparer, then I don't have to. We
16 defined it down to the level of consumer perception of
17 who's preparing the return and who is actually signing
18 it.

19 So if the CPA has six offices and they review
20 and sign every return, then their employees don't have
21 to be registered with CTEC, but if those employees sign
22 the return, then we expect them to be registered with
23 CTEC because we run into a lot of times -- the big one
24 for us is somebody will be sitting at a computer
25 terminal and saying I'm not preparing the return. That

1 computer prepares the return. So I don't have to be --

2 (Laughter.)

3 MS. MOORE: I don't have to be registered
4 with CTEC or anybody else because I'm not the preparer.
5 So what is the consumer's perception? The consumer's
6 perception is that you are preparing the return,
7 therefore you must be registered because we had
8 innumerable number of people trying to say they didn't
9 have to be registered because they just put it in.

10 MS. HAWKINS: Right. The degree of
11 creativity in this area is absolutely incredible.

12 MS. MOORE: It's incredible.

13 MS. HAWKINS: Yes, yes. Ron?

14 MR. WAGNER: As a point of clarification, we
15 do require all EAs to be licensed in Oregon by us, by
16 our Board.

17 MS. HAWKINS: And what about this firm
18 question?

19 MR. WAGNER: If it is a business, an EA owns
20 the business, everyone who prepares, advises or assists
21 in the preparation of the returns in that business must
22 be individually licensed, so that they do not fall
23 under the umbrella of the owner who's an EA.

24 COMMISSIONER SHULMAN: And do you know, Ron,
25 the distinction you made or who and when and why they

1 made the distinction between EAs and CPAs and attorneys
2 because you don't require CPAs and attorneys?

3 MR. WAGNER: That's correct. Well, that goes
4 back 37 years. So that's a difficult question to
5 answer. I really can only guess as to how that
6 happened. I'm just guessing that members of the CPA
7 community as well as the Oregon State Bar lobbied and
8 said we're already regulated under these umbrellas, we
9 don't need to be included in this group. I honestly
10 can't give an accurate response to that. It goes back
11 some time.

12 MS. HAWKINS: Jamie, you might want to add to
13 that because I know you all have the EA issue.

14 MS. WOODWARD: Right. Well, the EAs are required
15 to register with us because their lobby group isn't
16 quite the same as the other lobby groups, frankly. But
17 they are suing us, so their lawyers may be.

18 (Laughter.)

19 MS. HAWKINS: And I guess as clarification,
20 as well, for any of the EAs listening, Ron, as I
21 understand your exam, the EAs only have to take the 50
22 Oregon questions?

23 MR. WAGNER: That's correct. We assume that
24 an EA coming into Oregon has already proven their
25 competence regarding federal law. So what they do is

1 they take what we call the Oregon-only portion of our
2 exam which is the 50 questions on Oregon tax law and
3 state ethics.

4 MR. ERNST: So that's maybe a good jumping-
5 off point. I'm interested in your thoughts on how, if
6 we at the federal level had a system of either
7 registration or licensing or some combination, how you
8 would recommend we integrate that with what all of you
9 are doing at the state level or, alternatively, how to
10 structure something so that we don't have the level of
11 duplication that might otherwise occur at the state
12 level.

13 MR. WAGNER: First of all, I think that
14 registration is probably a good first step. I think
15 eventually, certainly we believe that the requirements
16 for some kind of a testing is certainly imperative to
17 test so we know that people are truly competent in what
18 they're doing.

19 If it was -- if it started out as
20 registration, we would continue with our program in
21 Oregon as it is. We would want to continue to make
22 sure that people are tested and show their competence.

23 If there is federal testing eventually, it's
24 difficult to say without knowing what that legislation
25 might look like, but I would venture to guess that we

1 would continue to test, if nothing else, just on Oregon
2 law because certainly it's wonderful that people have
3 knowledge on federal law, but they're also preparing
4 Oregon returns. They need to know the local state law,
5 as well.

6 So I would venture to guess that we would
7 continue to test just on state law and the state
8 ethics.

9 MR. ERNST: I also think it was you who said,
10 you know, in your comments that you believe whatever we
11 would do should include a portion on state issues.

12 MS. HERITAGE: Exactly. I mean, the CTEC
13 Board is really quite concerned that, you know, if
14 there is some type of federal program, perhaps there
15 would no longer be a CTEC, that, you know, there would
16 be no need, except that then what about the state tax
17 laws?

18 I mean, we feel that it's very important that
19 the people in California preparing have that, you know,
20 education in that. So we're not quite sure how but in
21 some way perhaps we would be like Oregon and just keep
22 CTEC and keep the 15 hours or 20 hours or whatever
23 we're going to require annually at that level, but at
24 this point we're not -- you know, we definitely want
25 something in there.

1 MS. HAWKINS: As a California practitioner, I
2 would just acknowledge that California's one of the few
3 states I know for almost the last 20 years that has not
4 routinely conformed to federal legislation which makes
5 it almost an entirely separate tax regime and a real
6 trap for the unwary outside of California, but with
7 respect to most of the rest of the states, you pick up
8 on virtually everything that we do at the federal level
9 in Title 26. So the dramatic differences are not
10 there, with the exception of California, I think.

11 MS. WOODWARD: We think it's very important
12 to have a national umbrella that covers minimum
13 requirements at the federal level and whether or not
14 that included state testing, I think that could be --
15 that's something that needs to be thought through
16 whether it should be a layered approach, but especially
17 New York, we're so close to California -- excuse me --
18 to New Jersey, Connecticut, Massachusetts, that those
19 borders for us are very problematic for different rules
20 and different states and as long as you have a basic
21 umbrella of competency or registration, at least, then
22 that allows us to have less duplication.

23 We're interested in streamlining this. We're
24 just starting. Maryland's just starting. If the IRS
25 sets up a program that, you know, Oregon and California

1 are the only two that have something else, we could
2 all, you know, leverage that instead of duplicate or
3 make conflicting rules. We'd like to see it. That's
4 why we're here is to say that we really need to
5 coordinate it and make it an integrated approach.

6 Now, also, while we follow on the income tax
7 area, we have a sales tax of which there is no national
8 IRS relation and we do have a lot of issues with our
9 sales tax preparers. We would see that as being a
10 separate, you know, focus for our part and not expect
11 you to be doing something there.

12 MR. ERNST: So this may be best directed
13 maybe to Wallace or, you know, the states that are just
14 recently coming into this. I'm interested in the kind
15 of hurdles you found in trying to both sort of develop
16 what a regime would look like but maybe as importantly
17 now, as you're in kind of the early stages of
18 implementing that, what kind of problems you've
19 encountered that might not have been anticipated,
20 funding maybe aside, but, you know, what problems
21 you've encountered so that, as we think about what we
22 might do, what, you know, kind of the practical
23 implications of that would look like.

24 MR. EDDLEMAN: I think for Maryland at this
25 point, it's funding only. We haven't gotten any

1 further than getting past the funding to start
2 anything.

3 MR. ERNST: How about the hurdles in getting
4 the legislation in the first place?

5 MR. EDDLEMAN: The legislation was supported
6 and, you know, was able to pass, you know, the House
7 and Senate and signed by the Governor. So I think
8 that, you know, with the amount of support it had, it
9 wasn't that difficult to get by from my knowledge.

10 MS. WOODWARD: Plus, I can tell you more in a
11 year from now. We are just starting in November, we'll
12 start the registration of the income tax preparers for
13 next year and some of our hurdles is just getting the
14 program up and running. It's a big project.

15 So we actually spread ours out because our
16 law does cross all taxes, but we are delaying the
17 business side of the tax registration for another year
18 to allow us to work on the tens of thousands of income
19 tax preparers as our first approach as those are the
20 most formidable clients served by that population.

21 But we did have an issue. We did have a \$100
22 registration fee for the commercial tax preparers.
23 That was a bit of an issue, but I have to say so far,
24 you know, the major tax preparation firms are
25 cooperating very well with us and we will see more in

1 November how many people actually register and we can
2 let you know later how that went.

3 MR. EDDLEMAN: One more comment on Maryland.
4 New York is much more broad. We only are -- our Act
5 only covers the individual tax preparation.

6 MS. HAWKINS: Mike, I'd like to go back to
7 you. You talked about the TIGTA shopping trips and
8 they seem to be quite productive for the state of New
9 York, as well.

10 But TIGTA does not have anything that I'm
11 aware of in its database now that shows shopping trips
12 where they may have gone out to check on licensed or
13 enrolled preparers. You've just looked at the
14 unenrolleds.

15 MR. McKENNEY: Right.

16 MS. HAWKINS: And so we don't really know
17 what the statistic might tell us if you took some more
18 shopping trips this busy season or something?

19 MR. McKENNEY: Right. There's no comparative
20 data and, you know, there's no guarantee it would be
21 significantly different.

22 MS. HAWKINS: And the data from each of you,
23 from GAO and TIGTA, you know, certainly is stark from
24 my perspective in terms of how many errors there are.
25 The data seems to encourage some kind of testing regime

1 or to ensure the competency level. Would you --

2 MR. McKENNEY: Especially in the area of what
3 we found was misinterpretation of the tax law which was
4 about two-thirds of the mistakes that we found, that
5 would help, and the ones, as I mentioned before, if
6 they were deliberate, I'm not sure the testing or
7 understanding of the tax law is really going to be a
8 benefit there.

9 But two-thirds, that would be a lot to solve
10 if some testing was put in place to make sure people
11 knew how to apply the tax law.

12 MS. HAWKINS: All right.

13 MS. WOODWARD: I also think to be fair to the
14 preparers, I don't think the states or the IRS have
15 been proactive in letting the preparers know what
16 errors were on their returns when we do a refund or a
17 bill goes to the taxpayer, not the preparer, so that
18 you're not really telling them what they need to know
19 or maybe they misunderstood something honestly.

20 So that we are working in New York to focus
21 on preparers and that's where the registration and the
22 numbering system becomes so helpful to us, is to
23 actually look at all the returns prepared by, you know,
24 Mr. X or Ms. Y and report back to them how did they do.
25 You know, are they commonly making a mistake on line

1 something or other? Are they misunderstanding? To
2 help educate them on a targeted area because even if
3 they go to continuing education, it might not be on the
4 topic they didn't understand, and I think we will be
5 pursuing that avenue, as well, as they are our partners
6 in this process and we should be giving them the
7 feedback that helps them educate themselves, as well.

8 MS. HAWKINS: Thank you.

9 MR. BROSTEK: One statistic that we've found
10 interesting in the Oregon data that's relevant to the
11 competency issue is that even after having taken the
12 required courses ahead of time, it was still, I
13 believe, only 54 percent of the test-takers for the
14 lower level license passed in the year that we analyzed
15 which means that 46 percent of those folks could have
16 been working in other unregulated states with not a
17 great amount of knowledge and the 54 percent passing,
18 getting three out of four questions correct, minimum
19 passing standard for 75 percent.

20 MR. WAGNER: If I can address that just
21 briefly, and that is the historical numbers, our Board
22 of Directors looked at that. We really wanted to see
23 if there was a way that we could increase the number of
24 people who are able to pass the exam, not by changing
25 the exam at all but recognizing that not everyone -- it

1 was mentioned earlier today that not everyone is a good
2 test taker and the test should not be about determining
3 who is good at taking tests. It should be about
4 measuring their competencies.

5 So back last November, we made a pretty
6 historic change that we now allow the test for the
7 entry level preparer, for that test to be taken open
8 book. We have a very specific list of items that are
9 able to be brought into the exam. They may not bring
10 any notes in, just the specified publications, and what
11 that allows them to do obviously is to be able to look
12 at where they are on the fence with the question.

13 The results of that is that it increased our
14 pass rate from about 54 percent up by 20 percentage
15 points. So since we put that into effect in December
16 1, 2008, that results show that our pass rate is now up
17 at about 73-74 percent.

18 We think that the benefit is that it's really
19 replicating what people do in real practice. What
20 people do is they don't memorize the Internal Revenue
21 Code, for heaven's sake. You can't. It's not to
22 determine who's good -- well, yeah, but exception here,
23 of course, but --

24 (Laughter.)

25 MR. WAGNER: It's not about measuring who's

1 got a good memory and who can memorize tables, but it
2 really replicates exactly what you do in real life and
3 that is you go to your source documents, you come to
4 your conclusion on tax law and how it applies to the
5 taxpayer.

6 So it's been very, very beneficial and we
7 think that it was a good decision. We have not made a
8 decision to allow the more advanced level which is the
9 licensed tax consultant. That exam is not open book.

10 MR. ERNST: Can I maybe shift to a different
11 topic, which one of the concerns that we have is that
12 any structure that we might develop runs the risk of
13 forcing people or having people go underground, just
14 simply do returns without registering or without
15 following through on the licensing.

16 I take the point that said, well, maybe your
17 fellow practitioners will be a good enforcement
18 mechanism that way to identify that.

19 I'm curious in California and Oregon what
20 kind of enforcement resources are needed, given that
21 there must be a significant amount or some amount of
22 people who are identifying unenrolled, unlicensed
23 preparers and they need to report that some place and
24 somebody needs to take action against those people,
25 what kind of enforcement mechanisms you use to do that.

1 MS. HERITAGE: We have on our website items,
2 a non-compliant complaint form, and anyone that wants
3 to report an unregistered preparer can go to that
4 particular screen, put in the information regarding the
5 person they believe is preparing illegally and they do
6 not have to put in any of their information, and then
7 that goes directly to the Franchise Tax Board and
8 that's how we handle it, and then they confirm that the
9 person is either registered or not registered, and then
10 they put it on their list of people to visit when
11 they're in that area.

12 MS. MOORE: We only have one and a half
13 person that's on our enforcement team. So we visit --

14 MR. ERNST: It's a small state, though.

15 MS. MOORE: Yeah. Not very many preparers
16 either.

17 We visited just under a thousand preparers
18 this last year, but what we have found in the period of
19 time since CTEC put their website up for people to
20 verify, when we first go out and it wasn't up, people
21 didn't have as much Internet activity in their offices,
22 we'd get complaints from people in the area that
23 everybody else was not registered.

24 Now, with them being able to look that up,
25 that has gone away and it's really reduced that problem

1 for us of having to look them all up. So having --
2 that really brings out -- that's one of the real
3 benefits of having the look-up function because when
4 people are sort of spying on each other, saying that
5 person's not registered, they found, ooh, oh, they are,
6 because they'll have complaints, everybody else does a
7 bad return, I'm the only one that does a good return.

8 MR. WAGNER: The process is similar in
9 Oregon. We do have a complaint form on our website.
10 However, we handle our investigations inhouse. We have
11 one compliance officer on our Board and she
12 investigates unlicensed activity.

13 Unlicensed activity is probably one of the
14 most serious offenses and something that we take -- is
15 brought to the attention of the Board and our Board of
16 Directors and we actively pursue the cases that we
17 hear.

18 We have to say that the licensees in Oregon,
19 they are our eyes and our ears in the community because
20 they probably are going to find out about someone who's
21 preparing returns without a license before we will find
22 out. So we get information from our own licensees
23 about unlicensed activity.

24 MS. MOORE: We had that. Just building off
25 that, Northern California works very much that way.

1 When somebody comes into a community in Northern
2 California, it's very easy for them to identify that
3 there's somebody new on the block and they'll check and
4 make sure that they're registered and, if not, we'll
5 hear from them.

6 In Southern California, it's a very different
7 environment. When you have 40 or 50 preparers in one
8 block, it's amazing how many -- we leave the car behind
9 when we go and visit Southern California and we just
10 walk up and down the streets and it's not unusual to
11 find 20 or 30 preparers on the same street and the
12 comment about that they do two things. Many of those
13 preparers perform marriages, divorces, immigration, you
14 can buy your confirmation gown, you can -- I mean 20
15 different businesses all within one store and there's a
16 desk in there, income tax.

17 MR. WAGNER: One stop shopping.

18 MS. MOORE: One stop shopping. You can do
19 everything there.

20 MS. WOODWARD: Well, and I think that's where
21 the education of the taxpayer themselves eventually is
22 the key there because if you're having someone prepare
23 it, they need to be signing it, too, and perhaps even
24 changing what the responsibilities are, if there's
25 errors, in some format might be a way to motivate folks

1 to actually look and pay attention to that.

2 MS. HERITAGE: A few years back, CTEC did a
3 survey of our preparers and in that survey, we asked
4 the question, would you be willing to have a fee
5 increase if we could get -- this was before we actually
6 had enforcement, and I think 85 percent of the people
7 indicated that they would be absolutely willing for a
8 fee increase if it meant enforcement because they were
9 concerned that they were doing the right thing but the
10 person down the street wasn't and they wanted those
11 people out of business.

12 MR. ERNST: So I'm interested, Ms. Moore.
13 You know, the comment that, you know, all this is sort
14 of designed to get at the preparers who are, you know,
15 doing weddings and gowns and everything else and
16 preparing returns on the side, you know, and to get at
17 sort of the competence level of those folks.

18 Clearly, California has a system in place,
19 but in Southern California, we have -- we all know we
20 have a large amount of that kind of activity that
21 continues.

22 What do you think it is about the way you've
23 done things in California that hasn't necessarily
24 gotten to that kind of preparer behavior?

25 MS. MOORE: Well, amazing, over the years

1 we've seen those people becoming registered and one of
2 the things that we do find is that even though they get
3 a penalty and only about 25 percent of that gets paid,
4 the next year 75 percent of those people do get
5 registered. So we are getting those people's attention
6 that they do need to be registered.

7 We have done some walking up and down the
8 streets. In some years nobody was registered, and then
9 the next year they're registered. So we are making a
10 real dent in it. You know, none of us know how many
11 are unregistered preparers out there. That's the end
12 rub, but we do know that any time we go out there, CTEC
13 increases the calls -- the calls they get increases
14 dramatically and we do know that we are -- the word of
15 mouth is getting out there that we are actually out
16 there.

17 When we first started, people would go C
18 what? They didn't know that it existed. I met one
19 woman up in Hamilton City in Northern California who
20 probably said that she had not been to any continuing
21 -- she'd never heard of CTEC and had not been to any
22 continuing education since 1975. She got registered
23 the next year.

24 So, you know, as we all know, there's no
25 major Tax Code changes in that period of time.

1 (Laughter.)

2 MS. MOORE: She'd never even heard of the Tax
3 Reform Act of 1982. So we know that we have some
4 impact that way.

5 MS. HERITAGE: We always know where FTB
6 enforcement people are because the phones start
7 ringing. How do we become registered? I mean, it's
8 just a given. They'll call in a very down time, say
9 July-June, all of a sudden we're getting those just
10 swarm of calls, and it's we want to know how to get
11 registered. So it's the word of mouth and networking
12 especially in those communities, like Los Angeles.

13 Closing

14 COMMISSIONER SHULMAN: Well, listen. We're
15 going to need to -- we're out of time. So we're going
16 to wrap this up. Let me make just a couple comments.

17 First, I just want to thank you. You all,
18 especially the four states that are here, have been at
19 the forefront of thinking about these issues. We're
20 going to need to work together. It's very important
21 that the IRS, the whole Federal Government works with
22 the states on important and complicated issues like
23 this. So we're going to look forward to working
24 together.

25 Let me thank GAO and TIGTA who've done great

1 work on this over time and I found this discussion very
2 enlightening and very helpful.

3 I just want to reiterate what people have
4 really said here, which is, every adult American has to
5 at least understand taxes and figure out if they have a
6 filing obligation or not. We have an incredibly
7 complex Tax Code at the federal level, not to mention
8 the state level.

9 My favorite statistic is that the federal Tax
10 Code is four times as long as *War and Peace* and so when
11 I'm working I'm memorizing.

12 As people said here and because it's so
13 complex and because it's a requirement, a lot of people
14 that end up using preparers, in our estimate 90 percent
15 use preparers or software, and so we owe it to people,
16 if we're going to have a requirement, that we do what
17 we can to make sure people are getting good service and
18 as Ron mentioned, preparers deal with intimate
19 financial data and personal issues of American
20 taxpayers.

21 If a preparer doesn't prepare a return right,
22 it can be years later that we end up finding it. You
23 have penalties and interest stack up and so we all need
24 to be part of this dialogue.

25 I think our job at the IRS in this initiative

1 we've undertaken is to listen and learn which we're
2 doing now, to end up with some vision of where we think
3 the world ought to be, to weigh the benefits and the
4 burdens in all of the complicated issues, this isn't a
5 straightforward issue, and then to lay out a practical
6 multiyear roadmap of how we get to our vision,
7 recognizing that these things don't just happen
8 overnight, especially at the federal level.

9 So we're going to keep at it. We're going to
10 keep listening. We encourage people to give us more
11 comments.

12 Thanks to all of you for coming and thank you
13 very much to the panel for great, great comments and
14 insight.

15 Thank you.

16 (Whereupon, at 10:59 a.m., the forum was
17 concluded.)

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